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# THE JOURNAL OF POLITICAL ECONOMY

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## THE STATE BANK OF INDIANA.<sup>1</sup>

THE first constitution of Indiana (1816) forbade the establishment of any bank unless it should be a state bank with branches. But it confirmed the charters of the two banks already in existence—the Farmers' and Mechanics' Bank of Indiana, at Madison, and the Bank of Vincennes. The latter was in 1817 made a state bank. It was badly, even fraudulently, managed, and early in the twenties was closed up by a writ of *quo warranto*. The Madison bank also went out of existence about the same time. This left Indiana without banks, the circulation being supplied chiefly by the Bank of the United States.

The State Bank of Indiana was one of the results of Andrew Jackson's war upon the United States Bank. Numerous scattered references<sup>2</sup> indicate that it was because of the expected

<sup>1</sup> The material for this paper is drawn chiefly from the official Reports submitted to the legislature, and such matter relating to the Bank as appears in the Documentary Journal of the legislature, together with what collateral evidence could be obtained. Much remains to be desired. The books of the Bank, for one thing, are nearly all lost.

The banking history of Indiana previous to the passage of the national bank act may be roughly divided into three periods. The first, 1816–1834, is not here treated. The second, embracing the life of the State Bank charter, 1834–1859, is the subject of study. The third period, that of the “free” banks, overlapping the latter part of the second, began in 1852 and continued until the national banks arose. A study of this third period would be exceedingly instructive, for it presents two systems side by side—the one very gratifying in its results, the other most disastrous. But it is here simply referred to.

<sup>2</sup> *Report of the President of the State Bank*, Dec. 12, 1835; *Governor's Message*,

end of that "monster," and the consequent withdrawal of its circulation, that the first bill for a state bank was introduced into the Indiana legislature. To provide a safe currency and prevent the flooding of the state with the uncertain paper of her neighbors, it was thought necessary that Indiana should have a bank of her own. One or two attempts had been made to establish a state bank prior to Jackson's veto in July 1832 of the bill re-chartering the United States Bank. The veto, however, had the effect of turning attention more strongly to the need of a state bank. Hence the next annual session of the legislature was largely occupied with a bill to establish a state bank.<sup>1</sup> There was strong opposition and the measure failed. During the following summer a number of public meetings were held in favor of a bank, and there was even talk of re-convening the legislature at once to reconsider the subject.<sup>2</sup> When, therefore, the annual session was opened in December 1833, the Governor, in laying the matter before the Assembly, said :

If . . . you find the public wishes and interests demand a bank, in establishing it it will be for you to introduce the needful restrictions, checks and guards, to save it from political bias or influence, to prevent any abuse or excess on the part of the directors and others employed in the administration of its affairs, and to secure the public against the probability of ultimate loss.

1837-8; *Indiana Journal*, Dec. 29, 1832 (communication signed "Citizen"); *ibid.*, Feb. 18, 1832 (Editorial).

<sup>1</sup>A communication to the *Indiana Journal* at this time (December 29, 1832), signed "Citizen," is worth noticing. It urged the passage of the bank bill, stating that it had been discussed for some months in every quarter of the state and was generally desired by the people; that business was already much depressed; and that the bank was needed to prevent the collapse of credit upon the close of the United States Bank, which would compel the withdrawal from Indiana of about \$2,000,000 in four years, for which some substitute must be had.

<sup>2</sup>In Indianapolis the feeling was especially warm because of the action of Calvin Fletcher, then and afterward a prominent citizen, who represented the county in the legislature. It was said that his vote had defeated the measure. Being a conservative man, he had stood firmly opposed to what he considered an unsafe bill. But the people wanted more money at any cost, and he was loudly charged with having caused the ruin of the town's business. He therefore resigned his seat. Later events, however, justified his action.

The legislature of 1833-4 assumed a like conservative attitude. The bill was introduced into the house December 28, 1833, by Mr. Dunn, and into the senate about the same time. The debate was very spirited, and the scrutiny of the bill unsparing; it was subjected to very severe attacks, and numerous amendments were made. The chief point of attack seemed to be the number of branches, which the bill fixed at ten. Repeated attempts were made to reduce it to five, with the thought on the part of many that the fewer the branches the less the mischief to be done. The provision stood, however. The bill passed the house January 18, 1834, by a vote of 49 to 24. In the senate it was amended so as to agree in all important points with the senate bill, and then, on January 22, passed by a vote of 18 to 11. Because of a difference between the two houses as to the mode of electing the president, a conference committee was appointed. This committee, on January 24, reported a compromise, which was concurred in. On January 28, 1834, Governor Noble gave his signature, and the "Act establishing a state bank" went immediately into force.

#### THE CHARTER.<sup>1</sup>

The charter thus granted created a system of banks, to be known as the State Bank of Indiana, which was to discontinue its active operations January 1, 1857, but might remain in existence, for the purpose of winding up its affairs, until January 1, 1859. This system was to be composed of a State Bank and ten branches.<sup>2</sup> But the ten branches were really for most purposes ten

<sup>1</sup>For the full text of the charter see the Appendix.

<sup>2</sup>An eleventh branch was to be organized after one year, and a twelfth after three years. An act of February 6, 1837, made it the duty of the directors to locate not less than three nor more than four branches in addition to those provided by the charter, time and place to be at their discretion. Except as to the sixteenth branch, the bank gave its consent to this amendment on February 7, 1838. The thirteenth branch was in 1838 located at Michigan City. Funds for the others were never provided, and they were never organized. An act of January 31, 1842, created a seventeenth district; in this district, also, no branch was ever organized. An act of February 10, 1843, repealed that part of the act of February 6, 1837, that provided for the fourteenth, fifteenth, and sixteenth districts; it repealed also the act creating the seventeenth district. This left thirteen branches, which remained the permanent number.

independent banks, subject to a certain control by the State Bank; and the latter was really nothing more than a board (consisting of a president and four members chosen by the legislature, besides one member chosen by each of the ten branches) with restrictive and supervisory functions, but with little power of initiative. The State Bank was to keep an office at Indianapolis, but the banking powers granted were to be exercised "by and through her branches, and not otherwise."

Aside from the fact that the board of directors of the State Bank were to locate the branches, their power over the affairs of the latter was, indeed, in many ways great. They could limit and control the discounts of a branch after they should reach one and one-fourth times the paid-in capital; for cause they could suspend a branch, and even close it up entirely if its operations should endanger the interests of the other branches, or if after one year it did not pay a profit of 6 per cent. on the paid-in capital; they could equalize the public deposits among the branches; they could examine each branch as often as they saw fit, and were required to do so at least once in six months; they could require reports from branches as often as they pleased, but at least monthly; they could call on all the branches to make up any deficiency in the assets of an insolvent branch; they could regulate the elections for directors of the branches; they could regulate the dividends of the branches so far as to insure that the capital should not thereby be diminished and that a surplus fund of one-sixteenth the capital should be maintained; they were to keep the plates and print the notes for all the branches, the notes to be signed by the president of the State Bank; and they were to fix the number of directors for each branch from ten to thirteen — of which they were to appoint three.

Subject to these restrictions, the branches were to be free to conduct their business without control from the central board. As has been said, that board itself was to be chiefly composed of members chosen one each by the various branches, so that each might have a voice in prescribing the general rules for the conduct of all. Each branch was to elect its own board of

directors—except the three appointed by the state board. Each local board was to choose its own officers, and in general manage its own affairs. Whose notes to accept, what kind of security to demand, how much reserve to keep, what terms to exact—all these matters were to be within the discretion of the local board. The branch was therefore not a branch, in the sense that its officers were not agents of a parent bank, and its policy not entirely directed from the center. The stockholders of one branch were not, as such, stockholders in any other, and in the division of profits each branch was to be independent of all the others. The relations of the branches to the central board thus exhibited something of the nature of a federal union, with a large amount of local self government, but at the same time an efficient central supervision.

The relations of the state to the bank as a whole were to be somewhat similar. The president and the four directors on the part of the state, by virtue of being chosen by the legislature, the former for five years, and the latter for four each, were responsible for their actions to the state authorities. They were to conduct all the preliminaries of organization, and because of their longer term of office would in other ways have naturally a greater influence than an equal number of the directors chosen by the branches (whose term was one year), although the latter greatly outnumbered them. The bank was required to make an annual report to the legislature, as were likewise the branches, while the legislature might at any time appoint a special examiner, with full powers of investigation, any officer who should make a false statement or report being guilty of felony. If such an examiner should find that the charter had been violated, or the governor should have reason to think that it had, action might be brought for the revocation of the charter. As one guarantee against political intrigue, no person holding an office under the general government or the state of Indiana, and no member of the legislature, could be an officer in the bank or any branch.

The features of the system recited above show the extent of the power over the bank lodged in the state authorities, and the

power over the branches given to the board of directors of the State Bank. A strong motive for exercising these powers effectively was furnished by the state's share in the acquisition of the capital. The capital stock was to be \$1,600,000, in shares of \$50, distributed equally among the ten branches. The state was to own one-half of this, individuals and corporations the remainder.<sup>1</sup> Before any branch could commence business, \$80,000 must be paid in, in specie, \$30,000 by individuals and \$50,000 by the state. The balance was to be paid in two equal annual installments, likewise in specie. In two years from the beginning, then, the entire capital was to be paid up in "hard cash." The state's predominating interest is further seen in the fact that individual subscribers might borrow from the state for the purpose of paying their second and third installments—not the first. To secure the funds to make these loans, and to pay its own installments, the state was to sell 5 per cent. thirty-year bonds, to the amount of \$1,300,000. Among provisions intended to secure the creditors of the bank against loss, one naturally looks first to learn what was the liability of the stockholders. The wording of the charter upon this point does not seem perfectly clear; and, since no occasion ever came up on which it

<sup>1</sup>As a matter of course, when new branches were organized the capital was proportionately increased. But other changes were made in its amount. A law approved January 25, 1836, authorized an increase of the capital in each branch to \$250,000, besides the subscription that any congressional township might make. By the law approved February 6, 1837, one-half of Indiana's share in the surplus revenue of the United States (one-half being \$280,000) was appropriated to increase the state's stock in the bank. An act approved February 6, 1841, provided that, so fast as the debtors of the sinking fund should pay their debts, the commissioners of the sinking fund should invest the amounts so paid in bank stock, in the name of the state. By the provisions of an act approved February 15, 1841, the surplus revenue fund, the college fund, the saline fund, and the State Bank school fund were all to be called in and invested in bank stock. There is some doubt as to how thoroughly this was done in the case of the surplus revenue fund, inasmuch as that fund had been distributed among the counties, and whether or not it should be invested in the bank rested with them. (E. G. BOURNE, *Surplus Revenue of 1836*). The depression succeeding the crisis of 1837, however, rendered the increased capital superabundant; the result was an act (approved February 2, 1843) providing for "the reduction of the state and individual stock in the State Bank." From that time on the amount of the capital was fairly constant (about \$2,000,000).

was necessary to call upon them, it is hard to say what would have been the actual interpretation. As nearly as I can judge, however, they were liable to the amount of their stock. That is, after having paid up their subscriptions in full, they were still liable for an equal amount, in case of insolvency.<sup>1</sup> This provision was strongly reinforced by section 9, as follows: "The said State Bank and each and every branch thereof shall mutually be responsible for all the debts, notes, and engagements of each other." It was further provided (section 46) that the board of directors of the State Bank were to provide for paying the debts of any insolvent branch by calling on the other branches to contribute their proportions. In this connection it is to be remembered that each branch was represented on the state board. These arrangements insured a close watch on each branch by all the others.

In addition to these remedial provisions fixing the liability, the interests of creditors were further considered in certain restrictive and preventive requirements. Specie payments should never be suspended, under penalty of paying 12 per cent. interest on the obligation; dealing in merchandise, or doing anything but a strictly banking business, was prohibited; holding real estate, except what was needed in the conduct of the business or had been taken in satisfaction of a debt, was prohibited; no bank notes were to be issued of less denomination than five dol-

<sup>1</sup>By section 44, the board of directors of the State Bank are given power to appoint receivers for any branch that is insolvent or being mismanaged and to "sue for and collect . . . all contributions required from stockholders under the provisions of the one hundred and second section of this act, or so much as shall be necessary to meet the demands against such branch."

Section 102 says that, in case of fraudulent insolvency, when the assets do not cover the liabilities "the whole amount of the deficiency shall be assessed on the whole number of shares of the capital stock of said branch, and the sum necessary to be paid on each share shall then be ascertained, and each stockholder shall be liable for the sum assessed on the number of shares held by him not exceeding the nominal amount of such share, in addition to the sums paid or which he may be liable to pay, on account of those shares." Whether the liability would be the same in the case of insolvency not fraudulent is not clear; yet that seems to have been the intention. Hugh McCulloch (*Men and Measures of Half a Century*, p. 118) states that the liability of stockholders was equal to the par value of their shares.

lars ;<sup>\*</sup> notes were made payable at the branch where issued, and were to be signed by the president of the State Bank and the cashier of the branch ; notes were not to exceed in amount twice the paid-in capital ; debts owing *to* the bank as a whole were never to exceed twice the paid-in capital ; debts due *by* the bank as whole (exclusive of deposits) were not at any time to exceed the same amount ; and debts due *to or by* any branch (exclusive of deposits) were never to exceed that amount, except by permission of the state board. Certain minor restrictions were also provided, such as prohibiting loans on the security of the branch's own stock ; loans to persons in arrears ; indorsement for one officer by another ; dividends to delinquent stockholders or the transfer of their stock ; the taking of greater interest than 6 per cent. ; and discounts for the purpose of enabling stockholders to pay installments on their stock, or to withdraw the money after it had been paid. The bank being a monopoly, the attempt seems to have been made to so hedge about the business that it should be at the same time reasonable in its charges to the public, safe in its character, and profitable to the stockholders.

In order that the bank bonds might be promptly paid off at maturity, a sinking fund was to be established, consisting of the following items : (1) All unapplied balances of the funds obtained by the sale of the bonds ; (2) the sums received in payment of the loans made to stockholders, and the interest on such loans ; (3) the dividends on state stock, and the dividends on the stock of individuals who had borrowed from the state to pay their second and third installments, and had not yet repaid their loans. The principal and interest of this fund was to be set apart for paying off the bank bonds, and was not to be used for any other purpose until that had been done ; after that, it was to be a permanent fund, appropriated to the use of common schools. The sinking fund was to be lent on real estate security, and to be in charge of a board of commissioners of the sinking fund, composed of the president of the State Bank and the four

<sup>\*</sup>This was amended in 1841 so as to permit notes for amounts of one dollar and upwards.

directors appointed by the legislature. It was also the duty of this board to see to the prompt paying of the interest on the bank bonds. And they were required to make to the legislature an annual report of their operations.

There is strong internal evidence to show that this charter was adapted from that of the Bank of the United States. The two are in many respects very similar, especially in the restrictions on the business. For instance, both prohibited dealing in real estate; in both the debts were limited to a certain ratio to the capital; the penalty for suspending specie payments was the same—12 per cent. interest; and, in both, dealing in merchandise was prohibited, as was any greater interest than 6 per cent. Each permitted existence for two years after active operations had ceased, and each provided the same remedy for violation of the charter—namely, a writ of *scire facias*. In a number of particulars, however, this charter differs from that of the Bank of the United States, and in some it is, from an economic point of view, a decided improvement. A difference in structure—making the Indiana bank something absolutely unique—has already been spoken of, namely, that the latter system was not composed of a great central bank with a number of subordinate offices. This may be partly accounted for by the fact that conditions were different in different parts of the state, necessitating local independence among the branches, in order that each might adopt such a policy as would best enable it to meet the business needs of the surrounding community. For, aside from the fact that some of the branches were in river towns, some in the interior, and one on the lake, the southern part of the state was settled from the South and the northern from the East—the result being that the people were different.<sup>1</sup> Indiana's ownership of a greater proportion of the capital, also, naturally led to a greater share in the management; the proportion of state directors was larger. But the one point of difference in which the superiority of the Indiana plan is distinctly shown is the stringent requirement that the entire capital shall be in specie, and that one-half of the

<sup>1</sup> McCULLOCH, *Men and Measures*, p. 78.

amount shall be paid in before operations commence. The type of bank thus established was the predominant one in those days. Safety was sought by limiting the debts to some multiple of the capital. There was no compulsory reserve and no preferred claim on the part of the note-holders. Neither the safety-fund nor the collateral-security system of securing the notes had yet risen well above the horizon; the country had still to see the beauties of the New York free banking act. Indeed, it would be too much to say that Indiana was at that time ripe for the modern methods. When the discounts were made almost entirely by means of bank notes rather than deposit accounts, and the great bulk of the creditors were the note-holders, it would seem that the interests of the latter were sufficiently protected by making all the debts a claim against all the assets. At any rate, it was a type of bank which retained a high degree of perfection in Indiana until the passage of the national bank act.

#### THE ORGANIZATION PERIOD.

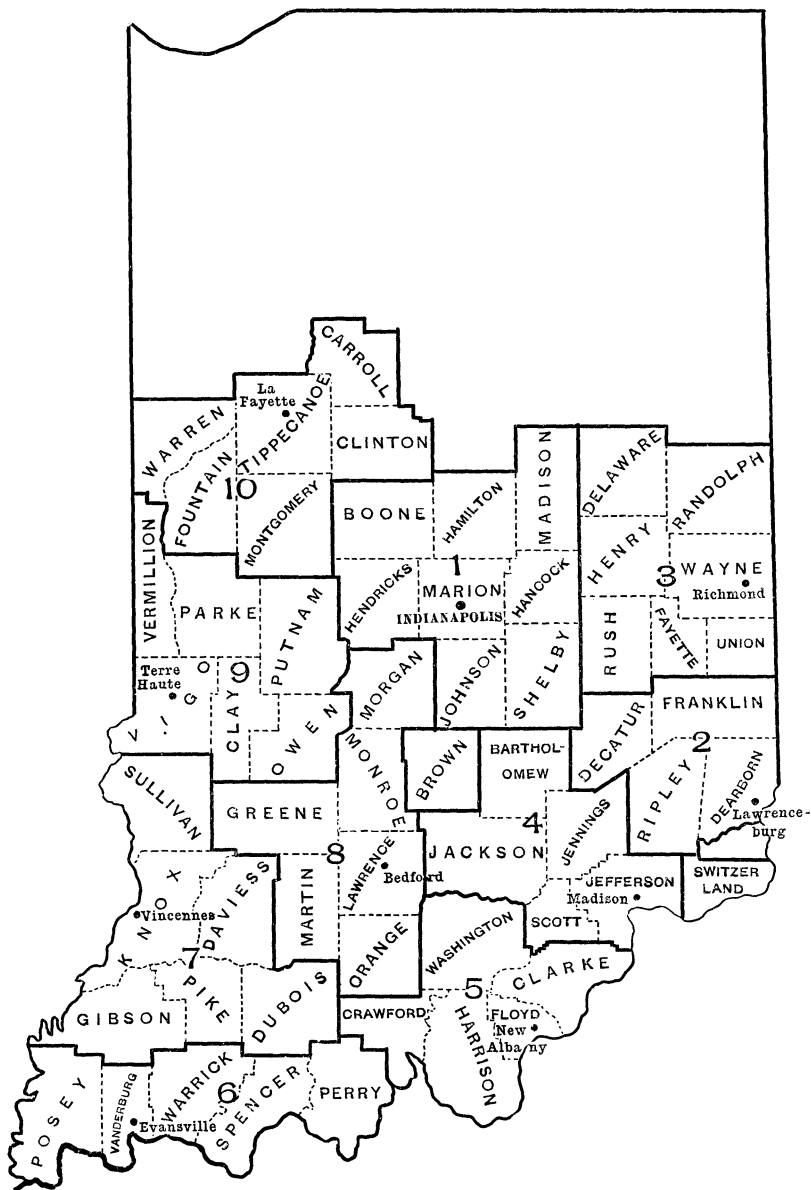
On January 30, 1834, the legislature elected the president and the four directors provided by the charter, as follows: President, Samuel Merrill, of Indianapolis; Directors, Calvin Fletcher and Seton W. Norris, of Marion county; Lucius H. Scott, of Vigo, and Robert Morrison, of Wayne. Mr. Merrill thereupon resigned the office of treasurer of state, which he had held for over ten years. These five men were to organize the bank. They met on February 13 and elected as cashier James M. Ray.<sup>1</sup> At this meeting the board located the branches at the following points: First district, Indianapolis; second, Lawrenceburgh; third, Richmond; fourth, Madison; fifth, New Albany; sixth, Evansville; seventh, Vincennes; eighth, Bedford; ninth, Terre Haute; tenth, Lafayette.<sup>2</sup>

<sup>1</sup> Mr. Ray was then auditor and recorder of Marion county, which office he resigned to accept the new one. As cashier of the State Bank he served throughout the existence of the institution, and then entered its successor, the Bank of the State of Indiana, in the same capacity.

<sup>2</sup> A glance at the map of Indiana on the opposite page will show the geographical distribution of the branches; four were on the Ohio, three on the Wabash, and three not on any navigable river, while all but two were near the boundaries of h

# MAP OF INDIANA

SHOWING BANKING DISTRICTS AND PLACES WHERE BRANCHES WERE LOCATED.



The books for the subscription of stock were opened April 7, and kept open for thirty days, as required by the charter. Subscriptions did not come in rapidly at first, but before the books were closed the stock was all taken at each of the branches. In the meantime the canal-fund commissioners (designated by the charter to negotiate the bank loan) had in March felt the pulse of the Eastern stock market. They had found it unfavorable, other states of established credit offering bonds without success. In July business had revived and 500 5 per cent. bonds of \$1,000 each (enough to pay the state's first installment of \$50,000 in each branch) were offered. In August they were sold to Messrs. Prime, Ward & King, of New York, at a premium of one and five hundredths (1.05) per cent.<sup>1</sup> The amount (in specie) was all in the hands of the commissioners before the fifteenth of October. The first installment of individual stock at all the branches was promptly paid in specie (mostly Spanish and Mexican silver dollars)<sup>2</sup> on the tenth of November. The next day the branches elected their directors. On November 19, 1834, Governor Noble issued his proclamation declaring the bank ready for business. About December 1, active operations were commenced, and on January 1, 1835, the loans stood at \$520,843.75; circulation, \$456,065; deposits, \$127,236.30; specie, \$751,083.29; capital paid in, \$800,000. Conditions were favorable and at the May meeting of the state board it was found that in the different branches the profits for the five months had averaged about 2½ per cent., though they varied considerably. No dividends were declared, but the entire amount credited to the surplus fund. In August 1835 bonds were sold by the state to the amount of \$450,000—\$400,000 for the second installment in the original branches, at 4½ per cent. premium, and \$50,000 for the first installment on state stock in the eleventh branch, at 5 per cent. premium. In 1836 the

state. This map also shows that the southern part of Indiana was settled first, and by people from the South.

<sup>1</sup> *Indiana Journal*, December 9, 1834.

<sup>2</sup> McCULLOCH, p. 119.

last of the state's bonds on account of the bank were issued. They amounted to \$440,000, and the money was paid to the president at New York on November 1, together with a part of the 1 per cent. premium. This made the bank loan \$1,390,000,<sup>1</sup> all of which was negotiated at a premium. November 25, 1835, the eleventh branch was established at Fort Wayne. The twelfth branch was located at South Bend, and authorized to commence business November 14, 1838. The thirteenth was located at Michigan City in 1838, but whether it began business in 1839 or 1840 is not to be determined from the reports. At any rate the annual report for 1840 gives the list of thirteen branches, and this was the number from that time on.

The heat generated by the Bank of the United States among national parties was reflected in the attitude of parties in Indiana toward the State Bank. Almost from the beginning there was a disposition on the part of Democrats to find fault, and on the part of Whigs to defend the bank with great acerbity. In the main this feeling was expressed only in talk. Occasionally the legislature might appoint a director with an eye to his political tendencies, yet the business was not interfered with. The most notable exhibition of party feeling was the deposing of Mr. Merrill, the first president. Mr. Merrill was a Whig, and the legislature of 1843-4 had, on joint ballot, a small majority of Democrats. His second term of five years expiring at this time, he was, after numerous ballots, defeated for re-election. Yet this display of partisanship luckily did not result injuriously, for the new president was Judge James Morrison, an eminent and able man. Mr. Morrison held the office until February 1853, when partisan feeling again asserted itself, and Ebenezer Dumont succeeded him. Mr. Dumont continued till the expiration of the charter.

<sup>1</sup> Several years later (1839), at a time when the state was going pretty heavily into the business of internal improvements, a large issue of bonds was made, \$1,000,000 of them being for the purpose of increasing the state's stock in the bank. But, because of the failure of the brokers to whom they were entrusted, the proceeds of these bonds never reached the state, and of course the bank's capital was not thereby increased, nor were the bonds considered "bank bonds;" they did not become a charge on the sinking fund.

The career of the bank may be roughly considered as comprising three periods: (1) 1835-6—a time of prosperity, perhaps more inflated than real; (2) 1837-43—a period of danger and great depression; (3) 1844-59—a period of real prosperity and smooth sailing.

#### THE SUSPENSION PERIOD.

The industrial and financial conditions of the country and of the state at the time of the organization of the bank were not conducive to sound banking. The multiplication of state banks, the rush for public lands, and the craze for internal improvements are well known as elements in the expansion preceding the great crisis of 1837. In Indiana the first of these can hardly have caused the others, for, as has been shown, the state was without banks prior to the commencement of business by the State Bank about January 1, 1835; and by the time the bank reached a position where it supplied anything more than the amount of circulation withdrawn by the Bank of the United States the bubble had expanded well towards the bursting point. But in the other two respects the people of the state must plead guilty. Only about fifteen years previously the site of Indianapolis had been chosen in an almost trackless wilderness. But during the first years of the bank the population was rapidly increasing and the lands were being rapidly opened up. The result, of course, was a lively demand for capital, both for buying and for improving the lands. In internal improvements, however, the aberration of the time is most distinctly seen. Plans were laid to gridiron the state with 800 miles of canals and 200 miles of railroads, to be built simultaneously, and to connect with like works in Ohio and Illinois; and in 1836 a loan of \$10,000,000 was authorized for the purpose. It was a grand scheme, but quite premature in view of the fact that the population was as yet less than 700,000, and that the state's resources were almost entirely undeveloped. When the collapse came, and the work was stopped, it was found that almost nothing had been completed, and that the entire system was well-nigh useless. The

worst result was that part of the state's debt was compromised at one-half, the creditors taking possession of the Wabash and Erie Canal in satisfaction of the other one-half. With industrial activities taking such a direction, it is almost a matter of course that the bank's business was affected for the worse. A large part of its funds was lent to buyers and improvers of real estate.<sup>1</sup> Bad as such loans always are for a bank, they were especially unsafe in this period of inflated values. Indeed, the bank managers themselves realized this fact.<sup>2</sup>

The justification for such loans was that at that time the industry of the state was predominantly agricultural, and that as yet its produce was not much in excess of the demands for home consumption; hence there was at first no demand for capital for commercial purposes, and a large demand for purposes of improvement. That this demand was largely speculative and premature is undoubted. Another influence aiding in the expansion of 1835 and the early months of 1836 was the bank's becoming one of the United States depositaries early in 1835. The government deposits had steadily increased until in January 1836 they had reached more than a million and a quarter. These funds of course increased the bank's power to make discounts, which in most of the branches reached the limit fixed by the state board—twice and one-third their paid-in capitals. But after January the deposits were for a time not increased, and even declined somewhat from the point they had at that time reached. About the last of April (apparently as a result of this

<sup>1</sup> McCULLOCH, p. 117.

<sup>2</sup> "It affords gratification to state that the business of most of the branches has been so conducted as to have no direct influence in raising the price of real property in their immediate vicinity; and it is believed that it has not been a leading motive at any of them to effect this object, and if, for want of other customers, too many loans have been heretofore made to speculators in land and town lots, this evil will soon be corrected. Business paper, more than can be discounted, is now offered to several of the branches, and at all of them a rapid increase of business, profitable to them and useful to the country, may be perceived." [Here follows a forecast of the probable course of speculation, significant in the light of later events.] "The bank may exercise an important influence in these matters by withholding its aid from all schemes uncertain in their result."—*Annual Report*, 1835.

condition of the deposits) the discounts ceased to expand, and the circulation began to be contracted.<sup>1</sup> This was before the issue of the specie circular of July 1836. By requiring public lands to be paid for in specie, that circular could not but affect the discounts of those banks that lent their notes to aid in buying lands. In September, moreover, more than half a million of the government deposits were withdrawn. After July, then, the contraction of the bank's issues was accelerated, and the amount of specie declined. After October, however, this movement was arrested and turned quite in the opposite direction by the payment of the final installment of the capital stock. Nevertheless, the expansion could not continue. In the last months of 1836 the government began to withdraw its deposits. As a result, even before the suspension of specie payments in 1837, the bank began to reduce its discounts. When the crisis of that year reached its height, and the state board learned that practically all the banks of the country had suspended, they at once advised the branches of the State Bank to do the same.<sup>2</sup> This

<sup>1</sup> See Chart I., showing Immediate Liabilities and Cash Resources of the State Bank of Indiana, for one day in each month. This chart is based on the figures of Table I., Appendix, pp. 109-113.

<sup>2</sup> The motives which influenced the board to take this action, and the facts they adduced in justification of it, cannot be better stated than in the words of the president, in his report to the legislative session of 1837-8:

"No act of the state board has ever impressed them with a deeper sense of responsibility than that by which they advised the branches to suspend specie payments. They were in session on the eighteenth of May last when information reached them that nearly all the banks in the United States had closed their vaults. The balance due this institution from other banks, and their paper then on hand, amounted to \$1,102,858.56. This sum would have been totally unavailable while specie payments were continued, and our bank must either have followed the example of others, or permitted the brokers and bankers of other states, the first informed and most active in these matters, to drain it of its specie, leaving the citizens of the state and large deposits due the general government unpaid, until collections of the notes and bills discounted could be made in specie funds, and until the banks could be compelled to pay what the public seemed to sustain them in refusing. If the \$5,311,804.97 then due the bank for loans and for notes, and balances on other banks, had all been pressed for at once, much of it must have been sacrificed, many of our best citizens ruined, and the industry and enterprise of the state must have been paralyzed for years. . . . A sudden reduction of the circulation of the state from about four millions of dollars to less than one-fourth that amount must have occasioned the depreciation of

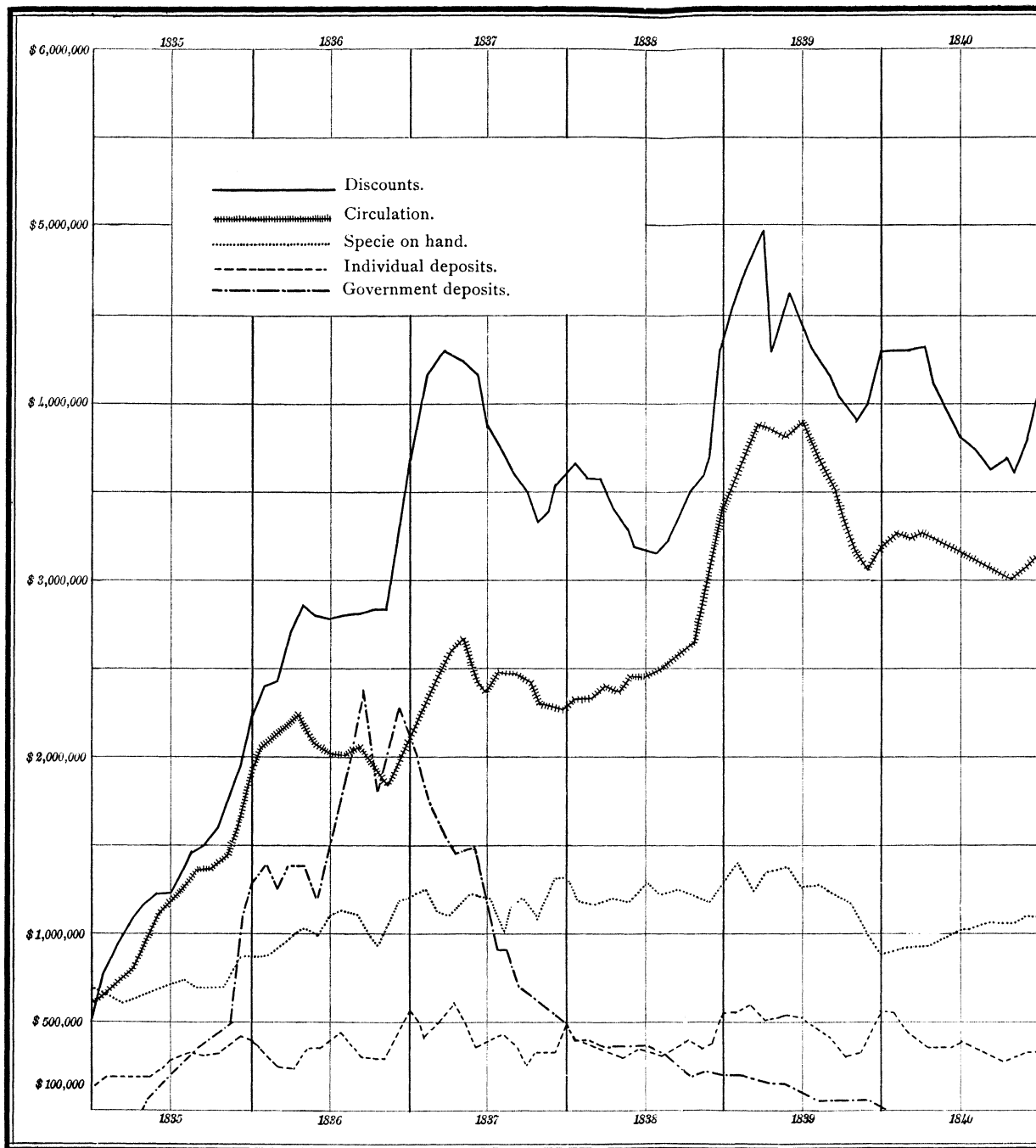
action received very general approbation from the people. A number of meetings were held in the state, and resolutions passed supporting the bank in what seemed the only possible course. A meeting of merchants at Indianapolis, May 19, agreed to take at par the paper of each branch of the bank. At a meeting of citizens the same day and place, Mr. Lanier, of the branch at Madison (then a state director and later a member of the well-known house of Winslow, Lanier & Co.), stated, as showing the perfect solvency of the bank, that it had more specie in its vaults, in proportion to capital than any other banking concern in the country; that its means were more than adequate to meet all liabilities; and that nothing but self defense against unjust abstraction of its specie by other banks could for a moment induce the idea of suspension.<sup>1</sup>

The governor's message to the session of 1837-8 referred to the suspension and commended it. But the legislature considered the matter at great length, devoting a very large part of its time to the subject. The final outcome was that the select investigating committee of the house reported<sup>2</sup> that the charter had been violated, but that it was inexpedient to have it revoked.

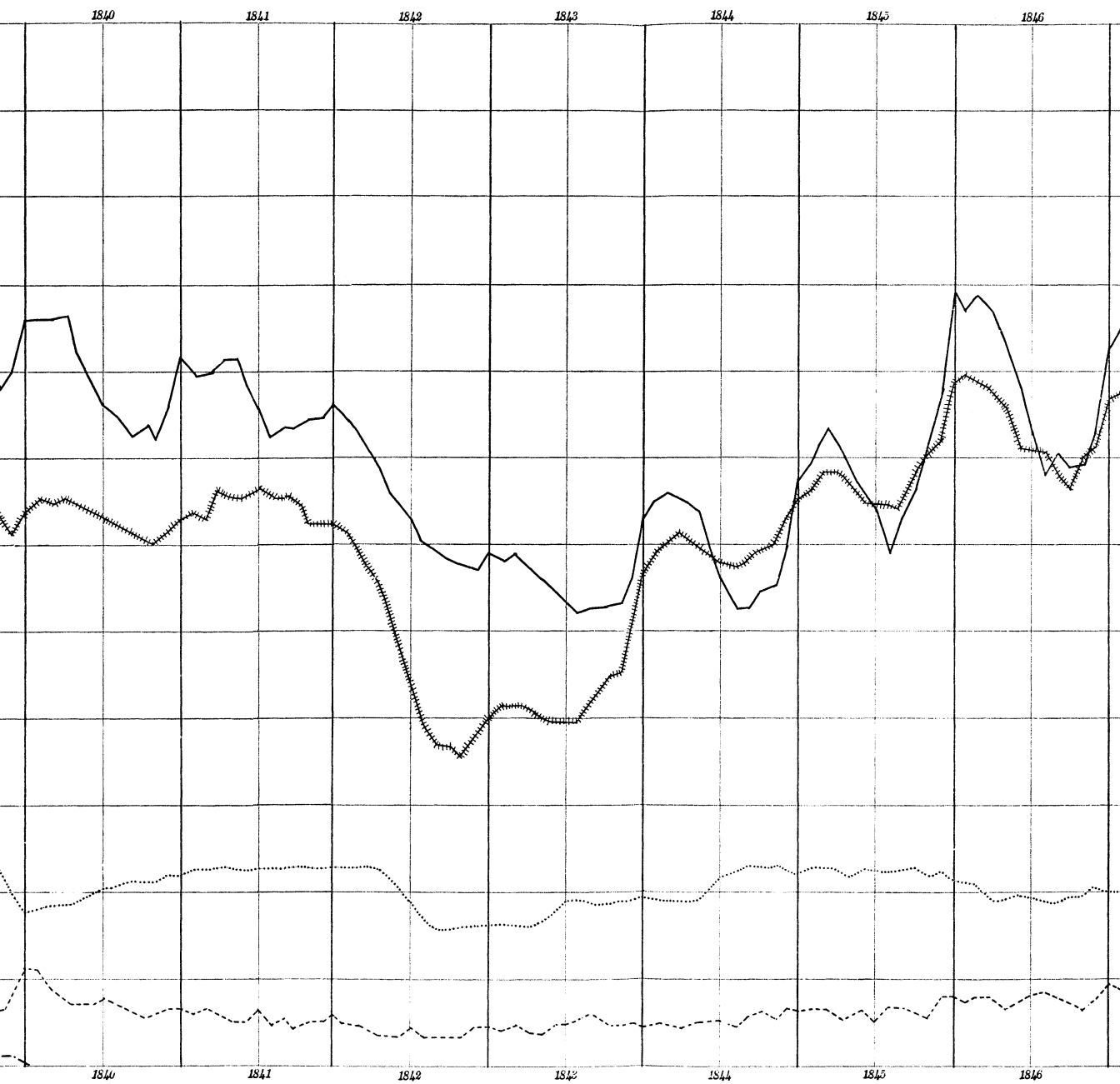
the value of property in about the same proportion. The sixteen millions of dollars estimated to have been due at that time by the citizens of the state to the bank, to the different loan offices, to foreigners and to each other, would have been collected, or attempted to be, in a medium made four times more valuable than that in which it was contracted." But by pursuing the course it did the bank "paid off \$761,920.13 of the debt to government, \$288,085 of notes in circulation, and \$106,994.69 of individual deposits, while the amount of specie decreased only \$58,162.87, all of which has been paid to government or for change. Few new debts have been contracted in the state, the old ones have diminished more than a fourth in amount, the paper of the bank is generally taken at par, and the confidence of the public in it and its officers has exceeded their most sanguine expectations. Only one doubtful debt to the bank, of \$400, is known to exist; but one person, and he is not now a resident of the state, has sued on its paper; and no doubt can exist in the mind of any intelligent citizen, but that specie payments can and will be resumed, whenever well-advised public opinion shall demand it."

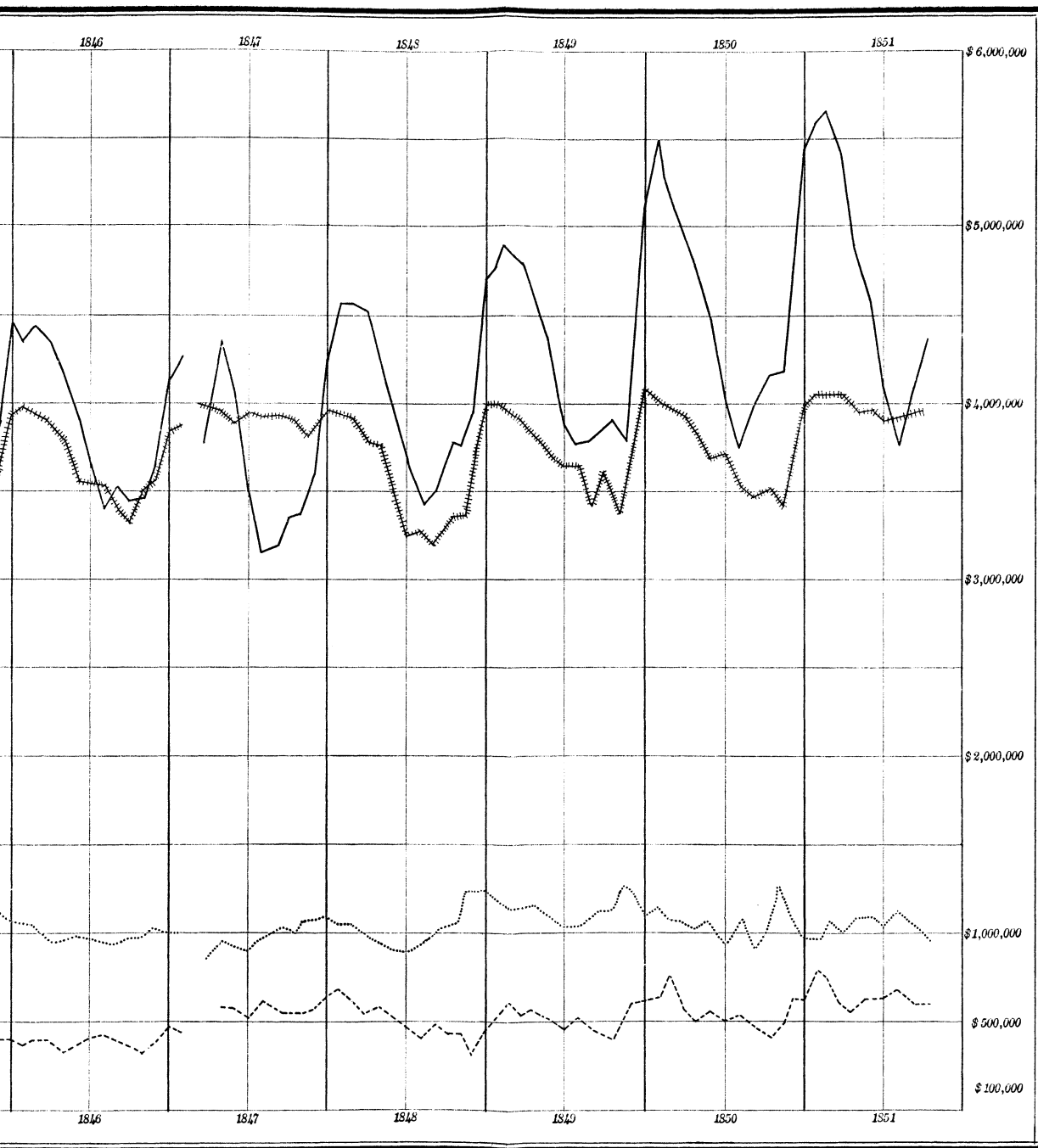
<sup>1</sup> The suspension was not absolute. In a communication to the *Indiana Journal* of June 10, 1837, Mr. Merrill stated that "deposits intended to be paid in specie are still so paid." McCulloch also (p. 119) states that the bank continued to pay out specie for small change.

<sup>2</sup> Mr. JUDAH'S *Report on the Suspension of Specie Payments*, January 1, 1838.



# CHART I.





The committee were "very unanimous" in refusing to recommend revocation, because the circumstances were well known, and the bank was considered necessary to public prosperity. But they agreed in recommending an amendment to the charter which, besides ordering resumption after a certain time, provided that any future suspension should be in itself a forfeiture of the charter. There was no doubt as to the solidity of the bank, and the legislature was evidently afraid that if it should be closed up the resulting contraction would only aggravate the existing evils.<sup>1</sup> The recommendation of the committee consequently came to nothing. The directors meantime had sent a delegate to a convention of bankers at New York looking toward resumption. This convention resulted in nothing definite. In April 1838 delegates were again sent to New York. This convention fixed upon the first Monday in January as the time for resuming, the Indiana delegates using their best efforts to secure an earlier day. The directors, however, endeavored by correspondence with western banks to have an earlier resumption agreed upon. In consequence of the discussion, a general resumption took place August 13, 1838, the Indiana banks accomplishing the fact with but little inconvenience.

During this suspension the discounts were contracted (circulation and specie remaining stationary), and the credit of the Indiana banks scarcely suffered. Indeed it was stated that the "notes of the State Bank of Indiana are in great repute, and command a premium at Nashville, Natchez, and New Orleans."<sup>2</sup> After the resumption the normal expansion of discounts and circulation in the winter and spring months took place, with the subsequent contraction in the summer. But the depression was

<sup>1</sup> The representative from Parke county, in an address to his constituents afterward published, says: "Although the investigation savored strongly of persecution, it resulted in everything the country could ask. It is certainly one of the greatest compliments . . . [that the bank] passed through the hands of a committee of so much talent, and a majority composed of the most implacable enemies to it that could be found in the state, and yet nothing was discovered calculated to raise a solitary doubt as to its perfect solvency."—*Indiana Journal*, April 14, 1838; reprint from the *Rockville Intelligencer*.

<sup>2</sup> *Indiana Journal*, July 7, 1839; reprint from Philadelphia *Public Ledger*, July 2.

not yet over, and in November 1839<sup>1</sup> the bank thought it necessary to again suspend payments, the branches this time not being advised to that step, but left to use their own discretion. There followed nearly three years of the deepest depression, commercially during which the bank was operating upon the very uncertain basis of a partial suspension. This condition seemed to be taken for granted, for the report for 1840 does not mention it. But in the report for 1841 the president says :

During the past year most of the banks in the western, middle and southern states have suspended specie payments. Ten of the branches of the State Bank, also, it is understood, have not uniformly paid specie on their notes when demanded, and probably the three others would have refused if their notes had been presented in large amounts from abroad. There have been, however, no protests of the notes of the bank ; no demands which have not been arranged ; no payment of the 12 per cent. penalty, except for very short periods, and no complaints to the state board of any one considering himself aggrieved in this respect by the branches.

It seems, though, that it did not much matter, because the energies of the community had been largely exhausted, and the business of the bank during this period was at a low ebb. But during the session of 1841-2 the legislature took the matter in hand, and by a joint resolution approved January 31, 1842, ordered the State Bank to resume specie payments by June 15, on penalty of forfeiting the charter. The *proviso* was made, however, that, if the banks of the surrounding states did not resume by that time, there should be no forfeiture for a refusal to pay specie to such banks, or to any person wishing to send it without the state "for purposes of traffic." In compliance with this order, the bank resumed on June 15, 1842, and never again defaulted. For several months previous to that day the officers of the bank had been preparing for resumption by redeeming its notes found in the cities on the borders of the state, wherever they were not in actual circulation.<sup>2</sup> The like was done to some

<sup>1</sup> President's reply (January 28, 1843) to certain resolutions of the legislature.

<sup>2</sup> *President's Report*, December 7, 1842.

extent within the state.<sup>1</sup> The result was that the resumption was effected with perfect safety to the bank. Whether it was also without great inconvenience to the people is not so easily determined, for the reduction in circulation was over a million and a quarter during the first ten months of 1842, while the loss of specie was only about \$350,000. Yet one feels inclined to say that resumption at any cost was better than the previous condition, and it is hard to see how it could have been safely accomplished in any other way than by previously buying up the notes with such funds as would be accepted.

The legislature of 1841-2 must have been composed either of very energetic conservatives or of enemies of the bank; for, besides ordering a resumption, it exercised its right under the charter of appointing a special examiner. The agent appointed was Mr. Nathan B. Palmer, a prominent and competent man, and a Democrat. Perhaps this last fact must be duly considered, in view of the differing attitudes of the Whig and the Democratic parties toward all banks, and of the fact that the president of the State Bank was a Whig. But after making all allowance for any possible prejudice that Mr. Palmer may have had, and for possible errors of judgment on his part, the report which he made to the legislature in December 1842 remains an able and exhaustive document. Beginning in April 1842, Mr. Palmer set himself to determine, "with all the care and scrutiny practicable," the exact condition of the bank and the causes which had "operated favorably or adversely" to its interests. "To this end," he says, "an absolute and actual count of all their cash, both coin and paper, has been had, together with an examination and scrutiny into all accounts with other banks, institutions and

<sup>1</sup> "We understand that Mr. Merrill, the president of the bank, is now visiting the different branches in the state, ascertaining their situation and preparing them for resumption. It is said he is also taking up all the Indiana Bank bills he can find either with brokers or business men, and paying for them with Kentucky or Southern funds. It has been stated to us that our banks are paying specie now in small sums for the accommodation of men and business, making the resumption gradual. But we can discern that their bills are retiring from circulation among us, and by August next there will be little or nothing in circulation among us, except Indiana treasury notes." —*Brookville American*; reprint in *Niles's Register*, April 2, 1842.

individuals—and the names, amount, and character of their bills receivable and other evidences of debts and credits, of every description, connected with the institution.” He concludes that “the State Bank at the period of this examination presents a favorable attitude, so far as regards a comparison of her present cash means with her immediate cash liabilities, but an unfavorable aspect in relation to the solvency and availability of the amounts due her on her discount line in both notes and bills.”

Mr. Palmer shows that the cash assets are equal to about one-half its immediate liabilities, three-fourths of the cash being actual specie. This he considers a safe condition. But as to total means he finds a deficit of \$333,422.03.<sup>1</sup> This result is reached by placing a much lower estimate on the value of the paper held by the branches than that made by their officers. With us, then, the question is to decide as to whose judgment was the better. In support of Mr. Palmer’s opinion it may be said that he was a clear-headed man, as the general impartial tone of his report shows; that his not belonging to the community whose paper he was examining left him in each case presumably without prejudice; that the officers of the branches, on the other hand, would naturally have a good opinion of the paper which they had accepted; that the collapse of prices after the crisis of 1837 must have depreciated the bank’s securities to a great extent; and that the “suspended debt” was for many years after a considerable item in the bank’s accounts. In support of the officers of the branches is their character, they being in general among the best and most capable men in their respective communities; their greater familiarity with local conditions, with the probability that they were better able than was the examiner to place a true estimate upon the ability of their debtors; and, not least, the fact that the ultimate result of the bank’s operations was such as to show it perfectly sound and to return to the stockholders a handsome profit.<sup>2</sup> It may perhaps be fairly concluded that the

<sup>1</sup> As the capital stock was \$2,731,357.14, a sudden closing of the bank would have necessitated an assessment on the stockholders of something over 8 per cent.

<sup>2</sup> Hon. Hugh McCulloch, then cashier and manager of the Fort Wayne branch, has

true position was somewhere between the two—that, while there was great truth in Mr. Palmer's statements, his estimates were somewhat too radical.

In discussing the causes of this unsatisfactory condition, Mr. Palmer was not disposed to criticise the bank adversely on account of the depreciation of its securities; he thought the most prudent business man could hardly have escaped with less loss. But upon one point he is severe; some of the branches had been in the habit of granting special favors to their stockholders and directors, in some cases allowing directors to retain their offices even after their notes had gone to protest. This practice he unqualifiedly condemns. He refers also to dealing in "fictitious" bills of exchange as a bad practice that had been indulged in to some extent.

The remedies suggested were very practical. The state owed the bank \$234,447.27 on account of advances made to contractors on the public works, besides which the bank held \$431,520 of sinking fund scrip, and \$264,080 of bonds, issued to it by the state for other advances. The total of these items was \$930,047. But the state's stock in the bank was considerably in excess of the amount required by the charter. Inasmuch, therefore, as the entire capital was much larger than what could be profitably used at that time, or could probably be used for several years, he suggested that the state redeem its obligations by surrendering part of its stock. He suggested also that the same plan be followed with those stockholders who had become delinquent debtors, the stock to be surrendered at its appraised market value. The legislature of 1842-3 accordingly passed a law (approved February 2, 1843), authorizing such a reduction of the stock. A law of February 11 also declared debtors to the bank ineligible to be directors or to vote for directors. With the accomplishment of these reforms, during the year 1843, the evil results of the prolonged suspension began to disappear, and the bank's troubles may be said to have ceased.<sup>1</sup>

very kindly responded to some personal inquiries, saying among other things: "We thought Mr. Palmer's report did not do full justice to the bank."

<sup>1</sup> Among other questions, Mr. Palmer asked the officers of each branch one con-

## THE FINAL PERIOD.

From this time (1843) the career of the bank was one of great prosperity, and there is little of special interest to record. During the latter part of the forties there was considerable opposition, which was reflected in that provision of the present constitution (framed in 1850-1) which forbids the state to hold stock in any corporation. One cause was the fact that the bank was regarded by many as a monopoly and an extortioner; and when the bank refused its assent to the organization of new branches, as it did,<sup>1</sup> this feeling was undoubtedly strengthened. The convention was probably influenced also by the state's internal improvement experience and by the example of other states in making like provisions.

The constitution of 1851 also permitted a free banking law. When such a law was passed in 1852, it destroyed the monopoly which the state bank had hitherto enjoyed, and from that time there was certainly plenty of capital devoted to banking in the state. There was some question as to whether the bank under its charter did not have the right to oppose the establishment concerning the premium on specie in the notes of the branch both before and during the suspension. Michigan City did not respond, and Lafayette reported that they "could not say" as to the time before the suspension, and that it varied at different points during the suspension. The others answered as follows:

			Before suspension.	During suspension.
Indianapolis,	-	-	Par	2-5 per cent.
Lawrenceburgh,	-	-	Slight	5-10 "
Richmond,	-	-	Par	2, 3-10 "
Madison,	-	-	Par	2-10 "
New Albany,	-	-	Par	2-7 "
Evansville,	-	-	Par	Av. 5 "
Vincennes,	-	-	Par	Av. 5 "
Bedford	{ at Louisville,	-	1-2	{ 5-6 "
	{ at other points,	-	1½-3	{ 6-7 "
Terre Haute,	-	-	Par	1-3 "
Fort Wayne,	-	-	Par	5-12 "
South Bend,	-	-	Par	5-10 "

*Niles's Register*, once or twice during 1839, in its quotations, gave Indiana notes at five to six per cent. discount in New York.

<sup>1</sup> *Annual Report*, 1849.

of these "free banks," and a nice constitutional controversy might have been raised about that point. But in view of the short time the charter had to run the officials decided not to contest the matter and to retire gracefully from the field at the end of their allotted time.

The last years of the bank were the most profitable, and when it ceased active operations it was in excellent condition. The results of the settlement of its affairs were very satisfactory. At two of the branches—South Bend and Michigan City—a final distribution was made before the first of January 1859; in eight of the others—Lawrenceburgh, Richmond, New Albany, Evansville, Vincennes, Bedford, Terre Haute, and Lafayette—sales were made of the remaining property and assets, and the business thus closed. But in three—Indianapolis, Madison and Fort Wayne—it was thought advisable to take a longer time in closing; their effects were therefore placed in the hands of assignees. A few items of the assets of the Vincennes branch, not included in the sale, were also assigned. The amount realized upon each share of stock of the par value of \$50 varied from \$58.50 at Bedford to \$90.53 at Lawrenceburgh, the average being \$76.85. Besides this there were certain sums realized upon the assets assigned by the four branches mentioned.<sup>1</sup> When the

<sup>1</sup> The rate per cent. of dividends for the different years was as follows, as given in the annual reports. The figures are averages of all the branches, which accounts for the fractions:

Per cent.			Per cent.			Per cent.		
1835	-	3.	1843	-	4.71	1850	-	10.
1836	-	9.36	1844	-	6.80	1851	-	9.35
1837	-	8.	1845	-	7.90	1852	-	9.35
1838	-	9.63	1846	-	....	1853	-	9.58
1839	-	....	1847	-	8.34	1854	-	12.
1840	-	....	1848	-	9.53	1855	-	15.77
1841	-	9.33	1849	-	9.80	1856	-	18.42
1842	-	7.						

For the years 1851 and 1852 in ten of the branches, and for the year 1853 in nine, dividends were made from the surplus fund that are not included. For the years 1854, 1855, and 1856 the figures include dividends from the surplus fund. The amounts are average dividends of all the branches; they therefore do not exactly show the profits on each share of stock, since the capitals of the branches were not equal.

business was about closed up, it was seen that a considerable amount of the circulating notes (in spite of repeated public notices to holders and of other efforts to bring them in) would still remain in the hands of the public after the bank was dissolved. At the close there were in circulation \$339,789 of the notes, out of \$4,208,725, the amount outstanding January 1, 1857.<sup>1</sup> In order to prevent the least stain upon its reputation, an estimate was made of the amount that might probably be brought in after the close of the bank, and contracts were made with competent brokers for the redemption of all that should be thus brought in. The plan worked well, and many notes were redeemed by these contractors, though many thousands were not presented for payment.<sup>2</sup>

#### THE SINKING FUND.

The sinking fund might be considered separately from the bank, as being simply the means adopted by the state for paying off the bank bonds and for profitably investing the state's dividends. The two institutions were in that sense entirely distinct. Yet they were complementary in their operations, for, while the aim of the bank was to base its business on short-time discounts and to steer clear of real-estate security, the policy of the sinking fund commissioners was to lend money on long time, secured by mortgage on real estate to twice the amount of the loan. To get the bank started, the commissioners of the sinking fund issued the bonds of the state for \$1,390,000, which were sold for specie, chiefly Mexican and Spanish silver. Of this amount \$880,000 was spent for stock on the part of the state. The rest was available for individual stockholders, who could borrow of the sinking fund for the purpose of paying the second and third installments on their stock. The state's profits from the bank were turned into the sinking fund. This fund was to guarantee the ultimate payment of the bank bonds, and also the

<sup>1</sup> *Report of the President*, January 7, 1859.

<sup>2</sup> Up to January 1, 1861, the contractors had cancelled notes to the amount of \$52,602.50.

prompt payment of the interest on them, which was regularly paid,<sup>1</sup> though the holders of other obligations of the state were not so fortunate. The fund could not be appropriated to any other purpose until the bonds had been paid. This was promptly done, some of them being taken up before maturity. The sinking fund was turned to productive use by being lent to the people of the state, and in later years was also largely invested in bonds of the state. In this way there was amassed, by the time the charter ran out, quite a large sum, which was to be set apart, after paying the bank bonds, as a permanent school fund. Although real estate values were greatly inflated during the earlier years, the commissioners were very careful and the fund never suffered any loss from bad debts. The fund and its profits, together with the amounts turned over by the nine branches that had closed business, amounted, at the time of the report of the commissioners on November 15, 1858, to \$2,780,604.36. There were four branches having assets yet to be converted, from which there was afterward realized \$79,296.10.<sup>2</sup> About one-half of this amount was due to the stockholders in those branches; the rest to the sinking fund, making the total amount realized from the bank and from the sinking fund during the lifetime of the bank something over \$2,800,000. This, however, was not the final amount. The fund could not be wound up at once, and therefore continued its operations for some years longer, with increased profit. When the sinking fund was turned over to the care of the auditor, on January 21, 1867, the statement of means and liabilities showed a balance in favor of the fund of \$4,647,016.17. In 1870 the auditor stated that the common school fund had up to that time received from the sinking fund about \$3,500,000 in non-negotiable 6 per cent. bonds. He says also that the fund has on hand or in process of collection over \$1,250,000, "so that by the time this fund is finally closed it will have added to the sacred

<sup>1</sup> *President's Report*, December, 7 1842; also the *Report* of December 30, 1856, "Survey of Operations."

<sup>2</sup> *Reports of Sinking Fund Commissioners*, 1859-66.

cause of common school education a permanent interest-bearing fund of nearly five million dollars." It needs to be said that of the amount still to be collected \$350,948.65, which had been distributed among the counties, might be hard to collect because of certain legal difficulties. This is as definite a statement of the profit to the state from the bank project as has been obtained, but it is doubtless somewhere near the ultimate figure, and we may be abundantly safe in saying that the amount realized by the school fund was largely in excess of three million and a half of dollars.

#### THE COURSE OF BUSINESS.

The community in which the State Bank of Indiana found itself was in 1834 almost exclusively agricultural. The need of credit for commercial purposes was therefore confined very largely to transporting the surplus produce of the farms. Another need was facilities for improving the land, for establishing such industries as there must be even in agricultural communities, and in general for opening up the resources of the state. At this period also the desire for great works of internal improvement was gaining ground. And doubtless the expectation that the bank would assist in the developing of resources, both public and private, had much to do with its establishment. This need for permanent capital was practically the same throughout the state, but the need for marketing facilities was not. "The pork season, when the great discounts are needed, comes on at the Ohio River in November and December, and on the Wabash in February and March, while in the interior the purchase of hogs and cattle for fattening is generally made still later, and the lake trade does not commence until a subsequent period."<sup>1</sup> The predominance of agricultural interests is further shown in the estimate made by Mr. Merrill that, throughout the state, population being about half a million, there were only about 900 persons engaged in merchandise, and an equal number in the river trade and as horse, cattle, and hog drovers, with a few manufacturers. The superior importance of

<sup>1</sup> PRESIDENT MERRILL, in a communication to the *Indiana Journal* of February 23, 1834, explaining the charter.

agriculture naturally had a great influence upon the subsequent policy of the bank.

At the beginning, then, the bank was likely to be called upon for loans from two different sources — from those who wished to market their produce, and from those who wished to sink capital in permanent improvements. The officers of the state board, however, clearly saw the danger in allowing the means to be used in making long loans. They declared the proper policy to be to make short-time loans based upon commercial transactions, and not to lend funds upon immobile security, or to suffer loans to be repeatedly renewed.<sup>1</sup> Here we have one of the fundamentals of sound banking clearly perceived. That the branches did to a considerable extent depart from this line of conservative action has been seen in treating of the period of the suspension. Perhaps under the circumstances they could have done no otherwise. Yet if their action was a necessity it was an unfortunate one, and the results we know. Experience, however, soon taught the necessary lesson, and with the revival of business after the resumption of 1842 the policy originally laid down by the president and state board began to be consistently carried out. About 1842 the policy was adopted of dealing more largely in bills of exchange than in promissory notes, with the result that the relation of the two items was soon completely reversed, so that, by the time the bank closed, its discounts were almost entirely composed of the former. The officers thought that by such a course they accomplished the double object of encouraging legitimate business and securing the safest and most profitable funds. This is the broad general fact in regard to the course of business operations which chiefly requires notice, and which probably gives some explanation of the great prosperity of the later years. But there are some other points requiring attention.

<sup>1</sup> The first *Annual Report* (December 5, 1834) contains the following: "To make loans for short periods, and for special purposes, and to require them to be paid punctually, will be found the most profitable to the bank, and the most useful to the country. This mode of doing business will keep out the paper of the bank; will bring in good funds; will accommodate the greatest number of customers; will suit the business of those who are taking the productions of the country to a market; and, by encouraging punctuality and regularity, will benefit the whole community."

Chart I. exhibits (for one date in each month) the items of discounts, specie, circulation, and deposits, from the beginning until the year 1851. By comparing the circulation with the deposits we see at once a very striking difference between modern banks in the United States and those of sixty years ago. We see that whereas at present bank credits are obtained almost exclusively in the form of deposits—simple credits on a book—at that day the reverse was true—bank credits were in the form of circulating notes. It will be seen that the correspondence between discounts and circulation is remarkably close, the latter rising and falling with the former, throughout the period here presented. The divergence of the two lines during the earlier years is doubtless because the large government deposits, which were used for discounting, were composed of various kinds of funds. The bank might therefore largely increase its discounts without increasing either its circulation or its individual deposits, and without decreasing its specie. It is thus clear that the use of deposit accounts as a credit function had practically no existence in this bank.<sup>1</sup> It is even doubtful that the deposits, small as they were, had the nature of credit; part of them, assuredly, were merely deposits of money for safe keeping. The fluctuations in the deposits after 1846 do indeed indicate that these accounts came more and more to be used in the modern way as means of discounting. During these years the fluctuations correspond in time quite closely to those in the discounts, indicating that the two were results of the same operation. Yet even at the last the deposits occupied a position of relatively little importance. We see, then, that this bank, quite in accord with the spirit of its time, was pre-eminently an issue bank.

The agricultural character of the state's industries explains another peculiarity in the bank's business—namely, that the discounts rose in the winter and fell in summer, being at their highest point usually in January or February and lowest in July or August. The pork season is referred to by the president as

<sup>1</sup> What banks of discount and deposit there were in the state of necessity so used deposits; but it is believed that their number was few and their business only a small fraction of the total banking business of the state.

the time when the greatest discounts were needed. Buying in the early spring, for fattening during the summer; shipping in the late fall; and packing in the winter — these various phases of the pork business seem to furnish the chief explanation of a thing which is just the opposite of present conditions, the discounts of modern banks reaching their highest point in midsummer. "Pork," then, explains this regularly recurring phenomenon.

The variations in the discounts over longer periods merit some further notice. There was a rapid expansion until 1837, when the suspension took place; a contraction of discounts (but not noticeably of circulation) then followed. When resumption was effected in 1838 the discounts again rose, but fell again after the second suspension, and continued to fall until after the permanent resumption of 1842, reaching their lowest point in the summer of 1843. The circulation, during both suspensions, remained comparatively on a level, while the discounts fell. These facts certainly do not show that in this bank a suspension loosened all sense of obligation, causing the necessity of ultimate payment to be lost sight of, and resulting in an expansion out of all proportion to cash means. On the contrary, the conservative character of the management as a whole is shown in the fact that contraction followed suspension, and expansion occurred only on a specie basis. After 1843 the discount line is seen to rise steadily until 1853.<sup>1</sup> During 1854 there was something of a financial flurry, when specie went East and there was a contraction of discounts. The entire course of the discount business would indicate that the crisis of 1837 exerted a very depressing and long-felt influence, but that when that was overcome the bank's career was one of continued prosperity. It will be noticed that from the early part of 1836 until the latter part of 1838 there is a considerable divergence between discounts and circulation that is not offset by individual deposits. But at the same time there were large government deposits on hand. These were used for discounting. If the government deposits furnished

<sup>1</sup>For annual data after 1851, see Table IV., Appendix, p. 114. Monthly data are available only up to October 1851.

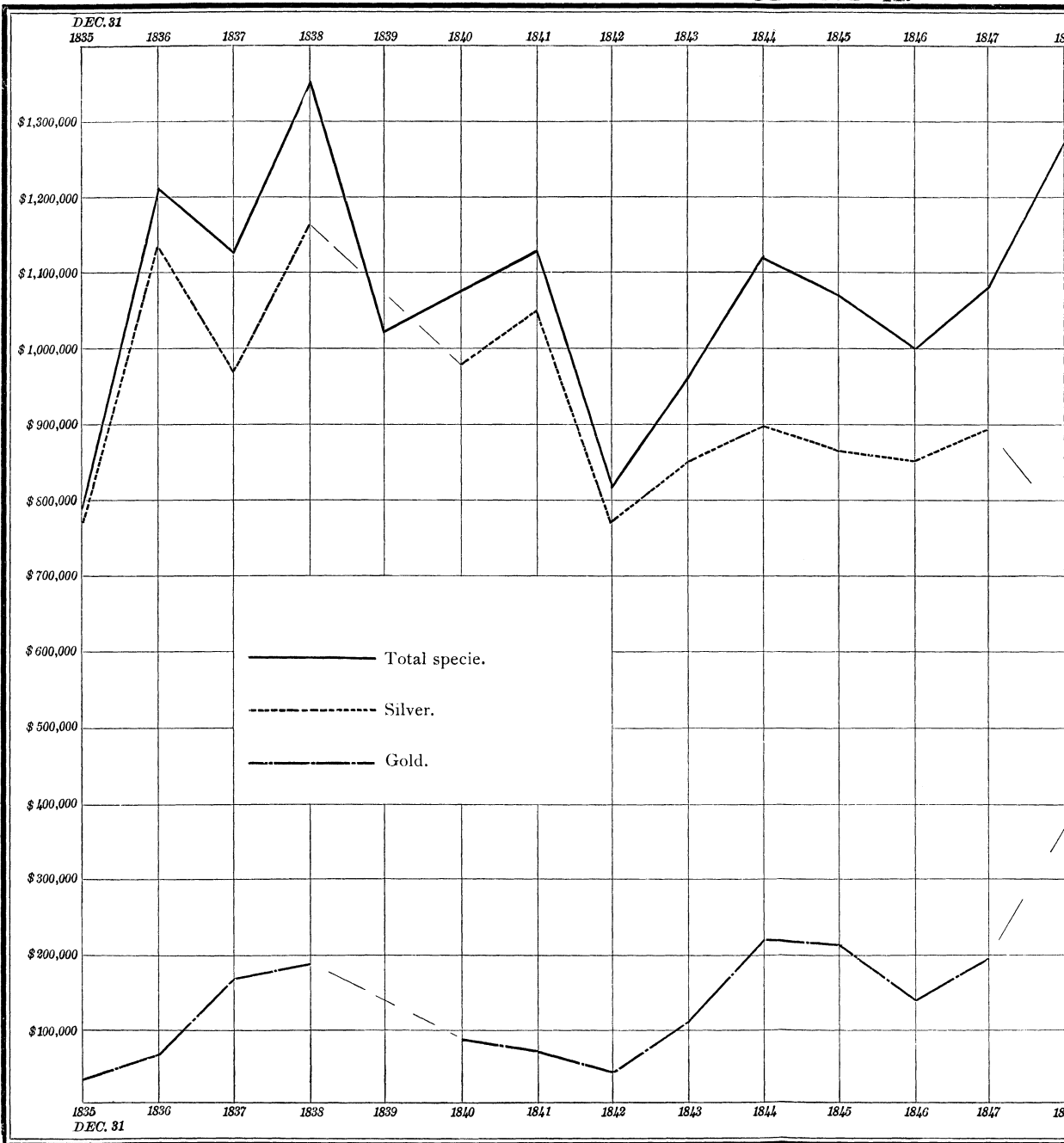
a means of discounting, they also formed a liability. How, then, did they affect the relation between immediate liabilities and cash resources? They were at their highest August 20, 1836, being then \$2,367,111.97. At the same date the circulation was \$2,032,235, and the individual deposits \$392,820.<sup>1</sup> Adding these, we have as the total of immediate liabilities \$4,792,167.04. At that time the specie on hand was \$1,102,595.12. This gives the actual specie means as 24 per cent. of the immediate liabilities. The city banks in the present national bank system are required to keep 25 per cent. of reserve in *legal* money. The government deposits evidently did not endanger the safety of the bank.

Throughout the existence of the bank, the reserve, although not large, was fairly safe.<sup>2</sup> At any date during the first suspension the specie was considerably over one-third the sum of circulation and deposits. At the time during the first resumption when the circulation was highest (June 29, 1839) the sum of circulation and deposits was \$4,485,412.38. Specie on hand being at the same time \$1,317,878.50, it amounted to 29 per cent. of the immediate liabilities. At no time during the second suspension was the ratio less than 24 per cent., while during the greater part of that period it was in the neighborhood of 30 per cent. Immediately after the final resumption of 1842, when the specie was at its lowest point, it was 39 per cent. Perhaps the time when the bank was weakest in this respect was January 31, 1851. The sum of circulation and deposits was \$4,818,290.29, while the specie was \$990,696.48—a percentage of about 20. We may be safe in saying that the bank never had specie to an amount less than one-fifth the immediate liabilities. This is less than the city banks are now required to keep; but the fairer comparison is with the country banks, which are permitted a reserve as low as 15 per cent. It must be remembered, too, that if we add to the specie the notes of other banks on hand (usually several

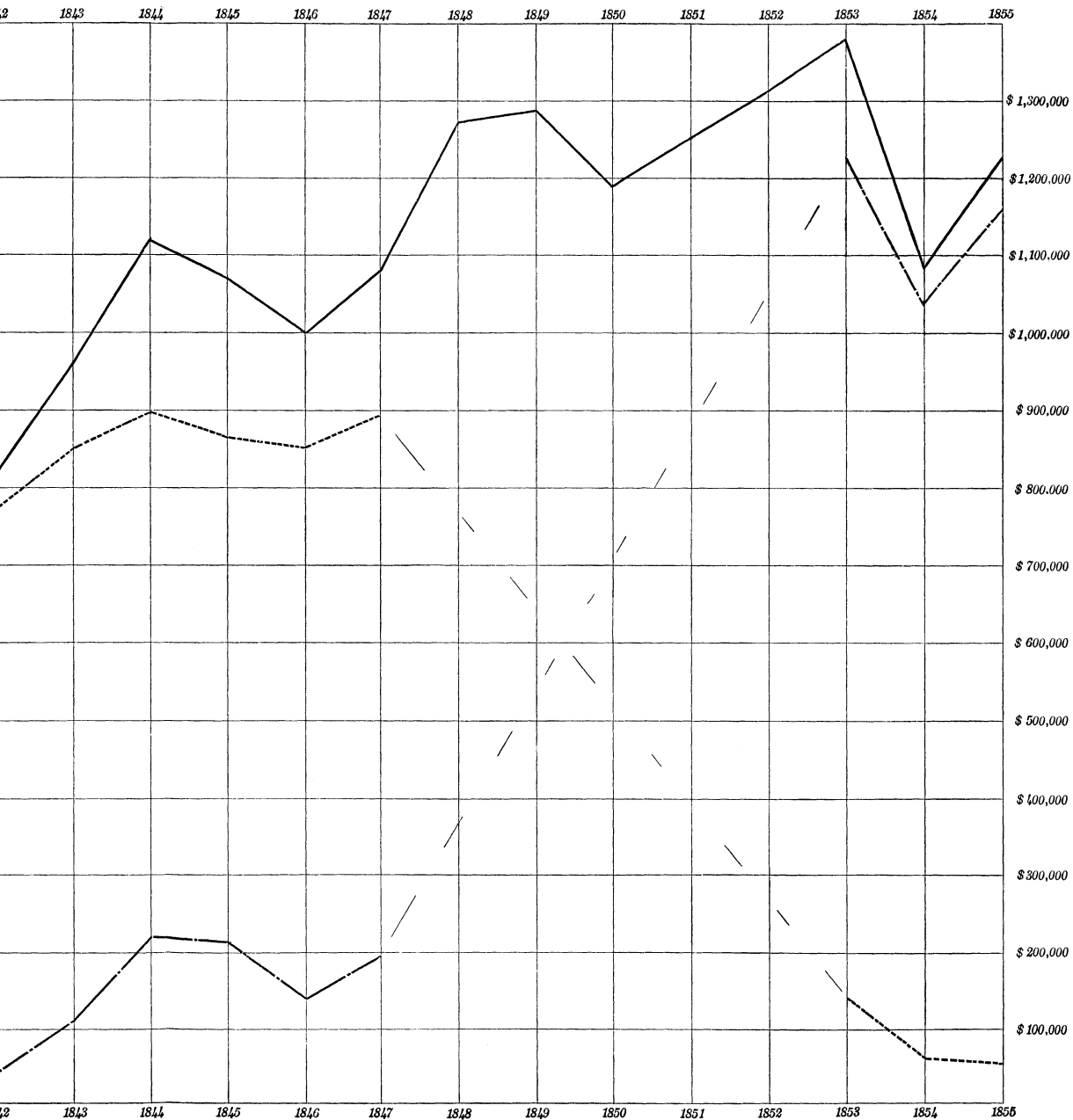
<sup>1</sup> See Chart I., and Table I. in the Appendix, p. 109.

<sup>2</sup> After 1851, however, the figures available are of little service in determining this point, being for only one date in each year.

# CHART II.



# CHART II.



hundred thousands) the condition is seen more favorably. And certainly we may make some allowance on that score, in view of the fact that the reserve of the national banks is not all hard money.

In this connection reference may be made in a general way to the relative amounts of gold and silver in the reserve. Chart II.<sup>1</sup> gives a graphic representation of these items for one date in each year until 1848, and also for the years 1853-6 inclusive. For the intervening years the specific figures have not been found. We see that at least as late as the latter part of 1848 the reserve was four-fifths silver, and in previous years had contained even a greater amount of silver. But in the last years given the reverse was true, and gold formed nine-tenths of the reserve. The exact date at which the transition took place is unfortunately not known. Mr. McCulloch states that the reserve continued to be in silver "until it was sold for gold at a premium of about 3 per cent. on Mexican dollars and 6 per cent. on Spanish," but does not tell us just when. It is of course a matter that does not materially affect the business of the bank, but it would be interesting from the point of view of monetary history to know whether this condition of the reserve was merely a result of the actual state of the currency in general,<sup>2</sup> or was due to inertia in the bank officials such as to overcome an overvaluation of gold, resulting from the change in the ratio made in 1834.

The amount of control actually exercised by the state board over the branches is shown by a couple of incidents occurring in

<sup>1</sup> Chart II., showing specie on hand, is based on the figures of Table II. (Appendix, p. 111), taken from the annual reports to the legislature, and shows the items as reported for one day in each year (usually the third Saturday in November). For 1839 and 1848-53 the reports do not give these items.

<sup>2</sup> MR. McCULLOCH (*Men and Measures*, p. 119) thinks that it was. He says that the coin "at that time was silver, and practically silver only. Although the double standard existed in the United States, the metallic currency of the country chiefly, and throughout the West exclusively, from the time the bank was organized in 1834 to the discovery of gold in California in 1848, was silver. . . . I had been a banker for fourteen years before I handled or saw a dollar in gold, except the ten-thaler pieces which were brought into this country by German immigrants."

1843. In the report for that year the president has the following to say: "The South Bend branch was for a time during the past year considered to be in an unsafe position. It was restricted in its discounts and required to make collections, which being effected, and the character of the officers of the branch being a guarantee that the privilege would not be abused, the transaction of bank business to a limited extent was again permitted."

Regarding the Lawrenceburgh branch, also, he says that there had been trouble with it almost from the first; that its officers and stockholders were granted large loans, many of which were allowed to stand for a long time without material reduction; that the state board had from time to time called attention to these evils; that from June 1842 to April 1843 the branch was in continual danger of failure; that various hazardous expedients were resorted to; and that when these were discovered by the examiners a change of policy was adopted, lasting from April to November, which was very unpalatable to many stockholders. Consequently, when the November election arrived, this dangerous element secured control of the branch. Other remedies having failed, the state board at its November session ordered, without a dissenting voice, that the branch be suspended. The suspension did not last long, however, for the branch was reinstated February 26, 1844. Were the facts easily accessible it would be very instructive to investigate the exact extent to which the state used the bank for its own fiscal purposes. It very evidently did to a considerable extent borrow from the bank—among other things, in anticipation of the fourth installment of the surplus revenue, which was never received. It also borrowed largely to pay the contractors on the internal improvements. The bank was at times seriously embarrassed because of these things.<sup>†</sup>

The State Bank of Indiana was a decided success, both from the point of view of the public and from that of the stockholders

<sup>†</sup> When the State Bank of Indiana ceased operations (January 1, 1857), it was at

It fulfilled the purpose of its creation in supplying to the public a safe and elastic currency to aid in conducting the business of the state and in supplying the need created by the withdrawal of the notes of the Bank of the United States. For the stockholders it was a very profitable investment. And the degree of efficiency attained by the common schools of Indiana is doubtless due in no slight degree to the large profit from the sinking fund. Two things perhaps contributed toward this success—the excellence of the charter and the excellence of the bank's managers. The points that contributed toward the excellence of the charter are numerous, and can hardly be briefly summarized; it was a system of many checks and guards. But three things stand out before all others. First and foremost is the mutual responsibility of the branches. Abundant latitude was left for them to manage their business in their own way, and for each to divide its profits independently of the others. But each was responsible for the debts of all the others; should one fail, without assets sufficient to pay its debts, all the others might be called upon to contribute their quotas toward liquidating the debts. The result was that each branch was alive to the manner in which every other was managed, so far at least as safety was concerned. The affairs of each were the business of all, and, as each had a voice on the state board, each was sure to exercise an effective vigilance over all. Secondly, the capital was paid in entirely in specie; this of itself was a guarantee of conservative management. Thirdly, the debts were limited to a definite ratio to the capital, as was also the circulation. These three things, I take it, are the most valuable provisions in the charter.

The officers of the bank were practically all entirely without once succeeded by the Bank of the State of Indiana, in which the state held no stock; in other respects the new bank was very similar to the old. The new bank (of which Hugh McCulloch was first president) was very successful until the national banks came; it then went out of existence.

In 1852 a free banking law had been passed, on the bond security system of securing the notes. The system of "free" banks was decidedly not successful in Indiana, whatever the reason.

experience in banking. From one point of view this very inexperience may have been the greatest element towards enabling them to successfully manage the business. For their inexperience was doubtless born of conservatism, and this conservatism of experience. Indiana's experience with its first State Bank, the Bank of Vincennes, was enough to show its citizens that banks cannot be run with wind or enthusiasm alone as the motive power. Hence they were quite willing for more than a decade to obtain their banking facilities through the United States Bank. And even upon the demise of that bank they were not wild to rush into the business; the stock of the State Bank was subscribed rather slowly. But if these inexperienced men were conservative they were also some of them very able—as, for instance, Hugh McCulloch and J. F. D. Lanier, both afterward occupying high positions in the financial world. The general fact is that the managers of the bank and its branches were among the ablest and most upright men of the community. It may be that men of high character could successfully manage a bank based upon any principles. What judgment, then, would our study lead us to pass upon a bank of this type, if we eliminate the character of the men? The type, be it remembered, is that of the Bank of France and the Bank of the United States. The Bank of France is certainly successful, and it will doubtless be generally admitted that the second Bank of the United States was on the whole a success, in spite of the great difficulties with which it had to contend and of its discreditable end. Here, then, we have three successful banks operating under widely different circumstances and managed by different men, but all based upon the principle of having all the debts a claim against all the assets. So far as the State Bank of Indiana goes, then, the inference is that there is nothing in the type of bank that makes it likely to be badly conducted.<sup>1</sup> It must be considered, also, that the bank had three different presidents, while the state board of directors were

<sup>1</sup>MR. McCULLOCH, in the letter before quoted, gives it as his opinion that "it would have required an immense amount of dishonesty or bad management to have made the bank insolvent."

being changed constantly, not to speak of changes in the branches. On the other hand, there is nothing in Indiana's experiment with the "free" banks to indicate that the principle on which they were based is any better; quite the reverse. It is of course true that for more than thirty years the entire tendency of banking movements in the United States was toward making the notes a preferred claim against the assets, and moreover against a certain portion of the assets, set apart in a particular form for the purpose of securing the notes. It goes without saying that the national banking system, the culmination of that movement, furnishes the country with the most reliable bank-note circulation it has ever had. But it is rather because of the absolute uniformity of the security throughout the country than because of the character of that security. No one, of course, would think of returning to the chaos that prevailed when each state had its own system. Yet it is by no means certain that the national banking system can be made permanent on the present basis of bond security. If, then, it become necessary to re-organize the system, it will be worth while to examine the merits of this Indiana system of federated banks.

Comparatively speaking, Indiana has been very fortunate in her experience with banks. Early in her history her fingers were burnt just badly enough to make her see and shun the fire. When, during the twenties, state banks were perhaps at their worst, Indiana had none, and was being sufficiently well served by the national bank. When the State Bank was established it was with the recent history of the successes and failures of other banks fresh in mind, and the fullest advantage was taken, in framing the charter, of that experience. The result was a system that furnished a sound currency until the Civil War. Even during the period of the "free" banks, the State Bank, and afterward the Bank of the State, was there, a standing judgment upon the notes of shaky banks. Indiana's one material failure, so far as banks are concerned, was in the case of these "free" banks. They were based upon the bond security system of the New York law; but because of defects in details, and insufficient

regard to the condition of the states whose bonds were accepted, the entire system was a failure. But this period lasted only from 1852 to the passage of the national bank law, and very few of the shaky banks were left after the panic of 1857. Thus Indiana had a sound institution to carry it over from the worst period of the state banks to the organization of the present national system.

WILLIAM F. HARDING.